

liabilities not represented by securities and which were incurred in the ordinary course of business before the reorganization does not prevent the application of section 354 to an exchange pursuant to a plan of reorganization defined in section 368(a)(1)(D).

(b) Except as provided in section 354 (c) and (d), section 354 is not applicable to an exchange of stock or securities if a greater principal amount of securities is received than the principal amount of securities the recipient surrenders, or if securities are received and the recipient surrenders no securities. See, however, section 356 and regulations pertaining to such section. See also section 306 with respect to the receipt of preferred stock in a transaction to which section 354 is applicable.

(c) An exchange of stock or securities shall be subject to section 354(a)(1) even though—

(1) Such exchange is not pursuant to a plan of reorganization described in section 368(a), and

(2) The principal amount of the securities received exceeds the principal amount of the securities surrendered or if securities are received and no securities are surrendered—

if such exchange is pursuant to a plan of reorganization for a railroad corporation as defined in section 77(m) of the Bankruptcy Act (11 U.S.C. 205(m)) and is approved by the Interstate Commerce Commission under section 77 of such act or under section 20b of the Interstate Commerce Act (49 U.S.C. 20b) as being in the public interest. Section 354 is not applicable to such exchanges if there is received property other than stock or securities. See, however, section 356 and regulations pertaining to such section.

(d) The rules of section 354 may be illustrated by the following examples:

*Example 1.* Pursuant to a reorganization under section 368(a) to which Corporations T and W are parties, A, a shareholder in Corporation T, surrenders all his common stock in Corporation T in exchange for common stock of Corporation W. No gain or loss is recognized to A.

*Example 2.* Pursuant to a reorganization under section 368(a) to which Corporations X and Y (which are not railroad corporations) are parties, B, a shareholder in Corporation X, surrenders all his stock in X for stock and

securities in Y. Section 354 does not apply to this exchange. See, however, section 356.

*Example 3.* C, a shareholder in Corporation Z (which is not a railroad corporation), surrenders all his stock in Corporation Z in exchange for securities in Corporation Z. Whether or not this exchange is in connection with a recapitalization under section 368(a)(1)(E), section 354 does not apply. See, however, section 302.

*Example 4.* The facts are the same as in *Example 3* of this paragraph (d), except that C receives solely rights to acquire stock in Corporation Z. Section 354 does not apply.

(e) Except as provided in §1.356-6, for purposes of section 354, the term *securities* includes rights issued by a party to the reorganization to acquire its stock. For purposes of this section and section 356(d)(2)(B), a right to acquire stock has no principal amount. For this purpose, rights to acquire stock has the same meaning as it does under sections 305 and 317(a). Other Internal Revenue Code provisions governing the treatment of rights to acquire stock may also apply to certain exchanges occurring in connection with a reorganization. See, for example, sections 83 and 421 through 424 and the regulations thereunder. This paragraph (e) applies to exchanges occurring on or after March 9, 1998.

(f) See §1.356-7(a) and (b) for the treatment of nonqualified preferred stock (as defined in section 351(g)(2)) received in certain exchanges for nonqualified preferred stock or preferred stock. See §1.356-7(c) for the treatment of preferred stock received in certain exchanges for common or preferred stock described in section 351(g)(2)(C)(i)(II).

[T.D. 6500, 25 FR 11607, Nov. 26, 1960, as amended by T.D. 7616, 44 FR 26869, May 8, 1979; T.D. 8752, 63 FR 410, Jan. 6, 1998; T.D. 8882, 65 FR 31078, May 16, 2000; T.D. 8904, 65 FR 58651, Oct. 2, 2000]

#### § 1.355-0 Outline of sections.

In order to facilitate the use of §§1.355-1 through 1.355-7, this section lists the major paragraphs in those sections as follows:

##### §1.355-1 DISTRIBUTION OF STOCK AND SECURITIES OF A CONTROLLED CORPORATION.

- (a) Effective date of certain sections.
- (b) Application of section.

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### § 1.355-2 LIMITATIONS.

- (a) Property distributed.
- (b) Independent business purpose.
  - (1) Independent business purpose requirement.
  - (2) Corporate business purpose.
  - (3) Business purpose for distribution.
  - (4) Business purpose as evidence of non-device.
  - (5) Examples.
- (c) Continuity of interest requirement.
  - (1) Requirement.
  - (2) Examples.
- (d) Device for distribution of earnings and profits.
  - (1) In general.
  - (2) Device factors.
    - (i) In general.
    - (ii) Pro rata distribution.
    - (iii) Subsequent sale or exchange of stock.
  - (A) In general.
  - (B) Sale or exchange negotiated or agreed upon before the distribution.
  - (C) Sale or exchange not negotiated or agreed upon before the distribution.
  - (D) Negotiated or agreed upon before the distribution.
  - (E) Exchange in pursuance of a plan of reorganization.
    - (iv) Nature and use of assets.
  - (A) In general.
  - (B) Assets not used in a trade or business meeting the requirement of section 355(b).
  - (C) Related function.
  - (3) Nondevice factors.
    - (i) In general.
    - (ii) Corporate business purpose.
    - (iii) Distributing corporation publicly traded and widely held.
    - (iv) Distribution to domestic corporate shareholders.
  - (4) Examples.
  - (5) Transactions ordinarily not considered as a device.
    - (i) In general.
    - (ii) Absence of earnings and profits.
    - (iii) Section 303(a) transactions.
    - (iv) Section 302(a) transactions.
    - (v) Examples.
  - (e) Stock and securities distributed.
    - (1) In general.
    - (2) Additional rules.
    - (f) Principal amount of securities.
      - (1) Securities received.
      - (2) Only stock received.
    - (g) Recently acquired controlled stock under section 355(a)(3)(B).
      - (1) Other property.
      - (2) Exceptions.
      - (3) DSAG.
      - (4) Taxable transaction.
    - (5) Examples.
    - (h) Active conduct of a trade or business.
      - (i) Effective/applicability date.

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### § 1.355-3 ACTIVE CONDUCT OF A TRADE OR BUSINESS.

- (a) General requirements.
  - (1) Application of section 355.
  - (2) Examples.
- (b) Active conduct of a trade or business defined.
  - (1) In general.
  - (2) Active conduct of a trade or business immediately after distribution.
    - (i) In general.
    - (ii) Trade or business.
    - (iii) Active conduct.
    - (iv) Limitations.
  - (3) Active conduct for five-year period preceding distribution.
  - (4) Special rules for acquisition of a trade or business (Prior to the Revenue Act of 1987 and Technical and Miscellaneous Revenue Act of 1988).
    - (i) In general.
    - (ii) Example.
    - (iii) Gain or loss recognized in certain transactions.
    - (iv) Affiliated group.
  - (5) Special rules for acquisition of a trade or business (After the Revenue Act of 1987 and Technical and Miscellaneous Revenue Act of 1988).
    - (c) Examples.

### § 1.355-4 NON PRO RATA DISTRIBUTIONS, ETC.

#### § 1.355-5 *Records to be kept and information to be filed.*

- (a) Distributing corporation.
  - (1) In general.
  - (2) Special rule when an asset transfer precedes a stock distribution.
- (b) Significant distributee.
- (c) Definitions.
  - (1) Significant distributee.
  - (2) Publicly traded stock.
- (d) Substantiation information.
- (e) Effective/applicability date.

### § 1.355-6 RECOGNITION OF GAIN ON CERTAIN DISTRIBUTIONS OF STOCK OR SECURITIES IN CONTROLLED CORPORATION.

- (a) Conventions.
  - (1) Examples.
  - (2) Five-year period.
  - (3) Distributing securities.
  - (4) Marketable securities.
- (b) General rules and purposes of section 355(d).
  - (1) Disqualified distributions in general.
  - (2) Disqualified stock.
    - (i) In general.
    - (ii) Purchase.
    - (iii) Exceptions.
      - (A) Purchase eliminated.
      - (B) Deemed purchase eliminated.
      - (C) Elimination of basis.
    - (f) General rule.

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- (i) In general.
- (ii) Purchase of additional interest.
- (iii) Purchase between persons treated as one person.
- (iv) Purchase by a person already treated as holding stock under section 355(d)(8)(A).
- (v) Examples.
  - (2) Transferred basis rule.
  - (3) Exchanged basis rule.
- (i) In general.
- (ii) Example.
- (4) Certain section 355 or section 305 distributions.
  - (i) Section 355.
  - (ii) Section 305.
  - (5) Substantial diminution of risk.
    - (i) In general.
    - (ii) Property to which suspension applies.
  - (iii) Risk of loss substantially diminished.
  - (iv) Special class of stock.
  - (f) Duty to determine stockholders.
    - (1) In general.
    - (2) Deemed knowledge of contents of securities filings.
    - (3) Presumptions as to securities filings.
    - (4) Presumption as to less-than-five-percent shareholders.
    - (5) Examples.
    - (g) Effective date.

### *§ 1.355-7 Recognition of gain on certain distributions of stock or securities in connection with an acquisition.*

- (a) In general.
- (b) Plan.
  - (1) In general.
  - (2) Certain post-distribution acquisitions.
  - (3) Plan factors.
  - (4) Non-plan factors.
- (c) Operating rules.
  - (1) Internal discussions and discussions with outside advisors evidence of business purpose.
  - (2) Takeover defense.
  - (3) Effect of distribution on trading in stock.
  - (4) Consequences of section 355(e) disregarded for certain purposes.
  - (5) Multiple acquisitions.
  - (d) Safe harbors.
    - (1) Safe Harbor I.
    - (2) Safe Harbor II.
      - (i) In general.
      - (ii) Special rule.
    - (3) Safe Harbor III.
    - (4) Safe Harbor IV.
      - (i) In general.
      - (ii) Special rules.
    - (5) Safe Harbor V.
      - (i) In general.
      - (ii) Special rules.
    - (6) Safe Harbor VI.
    - (7) Safe Harbor VII.
      - (i) In general.
      - (ii) Special rules.
    - (8) Safe Harbor VIII.
      - (i) In general.

- (ii) Special rule.
- (9) Safe Harbor IX.
  - (i) In general.
  - (ii) Special rule.
- (e) Options, warrants, convertible obligations, and other similar interests.
  - (1) Treatment of options.
    - (i) General rule.
    - (ii) Agreement, understanding, or arrangement to write, transfer, or modify an option.
    - (iii) Substantial negotiations related to options.
      - (2) Stock acquired pursuant to options.
      - (3) Instruments treated as options.
      - (4) Instruments generally not treated as options.
        - (i) Escrow, pledge, or other security agreements.
        - (ii) Options exercisable only upon death, disability, mental incompetency, or separation from service.
        - (iii) Rights of first refusal.
      - (iv) Other enumerated instruments.
    - (f) Multiple controlled corporations.
    - (g) Valuation.
    - (h) Definitions.
      - (1) Agreement, understanding, arrangement, or substantial negotiations.
      - (2) Controlled corporation.
      - (3) Controlling shareholder.
      - (4) Coordinating group.
      - (5) Disclosure event.
      - (6) Discussions.
      - (7) Established market.
      - (8) Five-percent shareholder.
      - (9) Implicit permission.
      - (10) Public announcement.
      - (11) Public offering.
      - (12) Similar acquisition (not involving a public offering).
      - (13) Similar acquisition involving a public offering.
        - (i) One public offering.
        - (ii) More than one public offering.
        - (iii) Potential acquisition involving a public offering.
      - (14) Ten-percent shareholder.
        - (i) [Reserved]
        - (j) Examples.
        - (k) Effective dates.

[T.D. 8238, 54 FR 289, Jan. 5, 1989, as amended by T.D. 8913, 65 FR 79722, Dec. 20, 2000; T.D. 8960, 66 FR 40591, Aug. 3, 2001; T.D. 8988, 67 FR 20636, Apr. 26, 2002; 67 FR 38200, June 3, 2002; T.D. 9198, 70 FR 20283, Apr. 19, 2005; T.D. 9264, 71 FR 30597, May 30, 2006; T.D. 9329, 72 FR 32799, June 14, 2007; T.D. 9435, 73 FR 75950, Dec. 15, 2008; T.D. 9548, 76 FR 65111, Oct. 20, 2011]

### **§ 1.355-1 Distribution of stock and securities of a controlled corporation.**

- (a) *Effective/applicability date of certain sections.* Except as otherwise provided, this section and §§ 1.355-2 through 1.355-4 apply to transactions